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**PAPER – 6E: GLOBAL FINANCIAL REPORTING STANDARDS**

*The question paper comprises three case study questions. The candidates are required to answer any two case study questions out of three.*

**Question No. 1**

- 1.1 *Monsoon Limited is engaged in the business of manufacturing sugar and chemicals. The Company has taken a term loan for ₹5 crores from SBI to buy certain plant and machinery during the year ended March 31, 2018. The loan is repayable over a period of 5 years.*

*The terms and conditions of the loan agreement requires the company to maintain a current ratio of 1.33:1 and debt-equity ratio of 1: 2. If these loan covenants fall below this level, then the bank has a right to recall the entire loan.*

- (i) *The Loan outstanding as on March 31, 2019 was ₹ 4.25 crores. The current ratio of Monsoon Limited was 1:1 and debt equity ratio was 0.5:2. SBI has sent a notice on April 5, 2019 demanding repayment of loan, on account of breach of terms of the loan agreement.*

*The financials were signed on May 10, 2019. How the long-term loan has to be classified in the financials for the year ended March 31, 2019?*

- (A) *Other current liabilities*
- (B) *Current financial liability*
- (C) *Non-current financial liability*
- (D) *Other non-current liability*

**(2 Marks)**

- (ii) *On receiving the notice, the CFO of Monsoon Limited negotiated with the bank and ensured to rectify the breach. As a result on April 25, 2019 the Bank has agreed not to recall the loan and allowed the Company to achieve the contracted current and debt-equity ratio by 2021. In that case, how the long-term has to be classified in the financials for the year ended March 31, 2019?*

- (A) *Other current liabilities*
- (B) *Current financial liability*
- (C) *Non-current financial liability*
- (D) *Other non-current liability*

**(2 Marks)**

- 1.2 *Saffron Limited is engaged in the business of manufacturing canned foods. During the year ended March 31, 2019 the company has decided to change its depreciation policy from straight line to units of production method for a more reliable estimate. How the change will be implemented in the books of more reliable estimate. How the change will be implemented in the books of accounts?*

- (A) *Retrospective restatement*

- (B) Prospective application
- (C) Retrospective application
- (D) Both Retrospective restatement and Retrospective application. **(2 Marks)**

1.3 Bharath Fabrics Limited is an 100% export-oriented unit. It manufactures fabrics in India and exports it to foreign countries all around the world. Its entire trade receivable consists of foreign currency receivables.

The Company has prepared its financials for the year ended March 31, 2019 and it is due for authorization in its annual general meeting scheduled to be held on June 20, 2019. The management of the company observed that there were abnormal fluctuations in foreign currency rates during April to June 2019.

As the CFO/auditor of the company suggest a suitable action from following:

- (A) Adjust the foreign exchange year-end balances to reflect the abnormal adverse fluctuations in foreign exchange rates.
- (B) Disclose the post- balance- sheet event in footnotes as a non-adjusting event.
- (C) Adjust the foreign exchange year-end balances to reflect all the abnormal fluctuations in foreign exchange rates (and not just adverse movements).
- (D) Ignore the post balance sheet event. **(2 Marks)**

1.4 India Turnings Limited has adopted revaluation model since 1<sup>st</sup> April, 2017 to measure its Property plant and equipment (PPE) and have revalued as follows:

- (i) As on April 1, 2017–PPE has been revalued up by ₹ 3,00,000.
- (ii) As on March 31, 2018–PPE has been revalued down by ₹ 3,60,000
- (iii) As on March 31, 2019–PPE has been revalued up by ₹ 5,00,000

How will the increase in year 2018-19 be recognized in the financials of India Turnings Limited?

- (A) ₹ 5,00,000 is credited to other comprehensive income.
- (B) ₹ 60,000 is credited to profit and loss account and ₹ 4,40,000 is credited to other comprehensive income.
- (C) ₹ 60,000 is credited to other comprehensive income and ₹ 4,40,000 is credited to profit and loss account.
- (D) ₹ 5,00,000 is credited to profit and loss account. **(2 Marks)**

1.5 (i) Terrain Industries Limited bought a private jet for the use of its top ranking officials. The cost of the private jet is ₹ 15 crores and has a composite useful life of 9 years. The engine of the jet has a useful life of 7 years. The private jet's tyres are replaced every 3 years.

*The Company is following straight line method of depreciation. What is the useful life to be considered?*

- (A) 9 years of composite useful life
- (B) 7 years useful life for the engine, 3 years useful life for the tyres, and 9 years useful life to be applied for the balance cost of the jet.
- (C) 3 years useful life, based on conservatism (the lowest useful life of all the parts of the jet).
- (D) 7 years useful life, based on simple average of useful lives of all major components of the jet. **(2 Marks)**

(ii) *Under the above same circumstances, what would be the useful life of the asset for the purpose of depreciation if the said company is following US GAAP?*

- (A) 9 years of composite useful life
- (B) 7 years useful life for the engine, 3 years useful life for the tyres, and 9 years useful life to be applied for the balance cost of the jet.
- (C) 3 years useful life, based on conservatism (the lowest useful life of all the part of the jet).
- (D) 7 years useful life, based on simple average of useful lives of all major components of the jet. **(2 Marks)**

1.6 *Global Limited, an Indian company acquired on September 30, 2018 70% of the share capital of Mark Limited, an entity registered as company in Germany. The functional currency of Global Limited is INR and its financial year end is March 31, 2019.*

(i) *The fair value of the net assets of Mark Limited was 23 million EURO and the purpose consideration paid is 17.5 million EURO on September 30, 2018.*

*The exchange rates as at September 30, 2018 was 82 INR/EURO and at March 31, 2019 was 84 INR/EURO.*

*What is the value at which the goodwill/capital reserve has to be recognized in the financial statements of Global Limited as on March 31, 2019?*

- (A) 451 million INR
- (B) 462 million INR
- (C) 451 million EURO
- (D) 5.50 million EURO **(2 Marks)**

(ii) *Mark Limited sold goods costing 2.4 million EURO to Global Limited for 4.2 million EURO during the year ended March 31, 2019. The exchange rate on the date of purchase by Global Limited was 83 INR/EURO and on March 31, 2019 was 84*

INR/EURO. The entire goods purchased from Mark Limited are unsold as on March 31, 2019.

Determine the unrealized profit to be eliminated in the preparation of consolidated financial statements.

- (A) 149.40 million INR
- (B) 151.20 million INR
- (C) 199.20 million INR
- (D) 201.60 million INR

**(2 Marks)**

- 1.7 An entity manufactures passenger vehicles. The time between purchasing of underlying raw materials to manufacture the passenger vehicles and the date the entity completes the production and delivers to its customers is 11 months. Customers settle the dues after a period of 8 months from the date of sale.

What is the Operating Cycle of the entity?

- (A) 11 months
- (B) 12 months
- (C) 19 months
- (D) 8 months

**(2 Marks)**

- 1.8 Evaluate following situations with reference to relevant standards:

- (i) Zest Limited is undertaking reorganization. Under the plan, part of the entity's business will be demerged and will be transferred to a separate entity, Zeal Limited. This also will involve a transfer of part of the pension obligation to Zeal Limited. Because of this, Zeal Limited will have a deductible temporary difference for the year ended March 31, 2019. It is anticipated that Zeal will be loss making for the first eleven years of its existence, but thereafter it will become a profitable entity. The future forecasted profit is based on estimates of sales to intergroup companies. Should Zeal Limited recognize the deductible temporary difference as a deferred tax asset?

**(2 Marks)**

- (ii) Dharam Limited has a subsidiary in USA consequently which adopts US GAAP. It has valued its inventory under LIFO method for Income Tax purposes. Discuss its implication both from the point of view of US GAAP and also from the point of view of its consolidation with the parent company which follows IFRS.

**(4 Marks)**

- (iii) Jeevan India Limited is in the business of development of smart city. For development of smart city, Jeevan India Limited allots its land to customer on 99 years of lease. The customer is required to pay lease premium at the time of execution of lease deed and lease rent on annual basis over a period of 99 years.

*The lease premium amount is the market value of land and lease rent is nominal amount say ₹1 per square metre per year. The lease premium is non refundable. As per the lease terms, on completion of 99 years, the lease is renewable at mutual consent of lessor and lessee.*

*How would income in respect of lease premium collected by Jeevan India Limited (which is the market value of land and is not refundable) at the time of execution of lease deed be recognized as per IFRS, if for subsequent years, only nominal lease rent is collected.* **(4 Marks)**

1.9 Comment on the following by quoting references from appropriate IFRS.

- (i) *Dong Seng Limited holds some vacant Land for which the use is not yet determined. The Land is situated in a prominent area of the city where lot of commercial complexes are coming up and there is no legal restriction to covert the land into a commercial land.*

*The Company is not interested in development the land to a commercial complex as it is not its business objective. Currently the land has been let out as a parking lot for the commercial complexes around.*

*The Company has classified the above property as investment property. It has approached you, an expert in valuation, to obtain fair value of the land for the purpose of disclosure under IFRS.*

*On what basis will the land be fair valued under IFRS?* **(6 Marks)**

- (ii) *Dong Seng Limited holds equity shares of a private company. In order to determine the fair value of the shares, the company used discounted cash flow method as there were no similar shares available in the market.*

*Under which level of fair value hierarchy will the above inputs be classified?*

*What will be your answer if the quoted price of similar companies were available and can be used for fair valuation of the shares.* **(4 Marks)**

- 1.10 (i) *Maroon Inc. Limited has received an exemption of customs duty on import of capital goods under Export Promotion Capital Goods (EPCG) scheme. The exemption is subject to an export obligation of 6 times of duty saved on capital goods imported under EPCG scheme, to be fulfilled in 6 years reckoned from authorization issue-date.*

*Whether the above scheme is a government grant under IFRS? If yes, then whether it is a Grant related to asset or Grant related to income. Discuss the way in which this has to be accounted for in the financial statements?* **(6 Marks)**

- (ii) *Croton Limited is engaged in the business of trading commodities. The company's main asset are investments in equity shares, preference shares, bonds, non-convertible debenture (NCD) and mutual funds.*

*The Company collects the periodical income (i.e. interest, dividend, etc.) from the investments and regularly sells the investment in case of favourable market conditions. Such investments have been classified as non-current investments in the financial statements.*

*Also, the company buys and sells equity shares of companies for earning short term profits from the stock market.*

*The CFO of the company classified all the non-current investments as Fair Value Through Other Comprehensive Income (FVTOCI) and all the current investments as Fair value Through Profit and Loss (FVTPL).*

*Croton Limited raised the following queries:*

- (a) Can the Company classify the equity shares previously held under current investment as FVTOCI if the company decides to hold them for more than one-year (i.e. classify it as non-current)?*
  - (b) The Company had classified NCDs with a maturity period of less than twelve months from the reporting period as current. This has been classified as FVTPL by the CFO of the company. The Company wants to know whether these NCDs can be recognized as FVTOCI?*
- (4 Marks)**

**Answer to Question No. 1**

- 1.1 (i) B
- (ii) B (as per IAS 1) or C (as per Ind AS 1)
- 1.2 B
- 1.3 B
- 1.4 B
- 1.5 (i) B
- (ii) A
- 1.6 (i) D
- (ii) A
- 1.7 C
- 1.8 (i) It might be difficult to place significant reliance on internal management projections where an entity will be loss making for the first eleven years of its existence. Projections become more subjective, the greater the period that is considered for sufficient taxable profits. However, if an entity is reliably able to project future taxable profits, then it can recognise deferred tax assets.

In the given situation, it is assumed that the future forecast of the entity to earn taxable profit on estimates of sales to intergroup companies is probable. Hence, the deferred tax asset could be recognised in the stand alone financial statements of Zeal Ltd.

However, in the consolidated financial statements of the group wherein Zeal Ltd. is a member, should not recognise the deferred tax asset as sales to inter-group company and profit thereon will be eliminated.

- (ii) Under US GAAP, a variety of inventory costing methodologies such as LIFO, FIFO, and/or weighted-average cost are permitted. For companies using LIFO for US income tax purposes, the book/tax conformity rules also require the use of LIFO for book accounting/reporting purposes. However, as per IFRS the use of LIFO is precluded.

Further, as per para 19 of IFRS 10, a parent shall prepare consolidated financial statements using uniform accounting policies for like transactions and other events in similar circumstances. As per para B87 of the standard, if a member of the group uses accounting policies other than those adopted in the consolidated financial statements for like transactions and events in similar circumstances, appropriate adjustments are made to that group member's financial statements in preparing the consolidated financial statements to ensure conformity with the group's accounting policies.

Since Dharam Ltd. is a parent company who will be preparing the consolidated financial statements as per IFRS, it has to remeasure the inventory of USA based subsidiary company as per the inventory method and accounting policies followed by Dharam Ltd.

- (iii) Paragraph 5 of IFRS 15 scopes out revenue arising from lease agreements. Principles enunciated under IAS 17\*, Leases would be applicable for revenue arising from leasing agreements.

Recognition of income in respect of lease would depend on its classification as per IAS 17, Leases.

If the lease of land is an operating lease, then it will be accounted for as given below:

- Lessors shall present assets subject to operating leases in their balance sheet according to the nature of the asset.
- Lease income from operating leases shall be recognised in income on a straight-line basis over the lease term, unless either:

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\* For May, 2019 examination, IAS 17 is applicable.



- (a) another systematic basis is more representative of the time pattern in which use benefit derived from the leased asset is diminished, even if the payments to the lessors are not on that basis; or
- (b) the payments to the lessor are structured to increase in line with expected general inflation to compensate for the lessor's expected inflationary cost increases. If payments to the lessor vary according to factors other than inflation, then this condition is not met.

The long lease term may be an indication that the lease is classified as a finance lease. If it is a finance lease then lessor Jeevan India Ltd. shall recognise assets held under a finance lease in their balance sheets and present them as a receivable at an amount equal to the net investment in the lease. The recognition of finance income shall be based on a pattern reflecting a constant periodic rate of return on the lessor's net investment in the finance lease.

Nominal lease rent collected every year will also be accounted every year on accrual basis.

- 1.9 (i)** As per IFRS 13, a fair value measurement of a non-financial asset takes into account a market participant's ability to generate economic benefits by using the asset in its highest and best use or by selling it to another market participant that would use the asset in its highest and best use.

The highest and best use of a non-financial asset takes into account the use of the asset that is physically possible, legally permissible and financially feasible, as follows:

- (a) A use that is physically possible takes into account the physical characteristics of the asset that market participants would take into account when pricing the asset (eg the location or size of a property).
- (b) A use that is legally permissible takes into account any legal restrictions on the use of the asset that market participants would take into account when pricing the asset (eg the zoning regulations applicable to a property).
- (c) A use that is financially feasible takes into account whether a use of the asset that is physically possible and legally permissible generates adequate income or cash flows (taking into account the costs of converting the asset to that use) to produce an investment return that market participants would require from an investment in that asset put to that use.

Highest and best use is determined from the perspective of market participants, even if the entity intends a different use. However, an entity's current use of a non-financial asset is presumed to be its highest and best use unless market or other factors suggest that a different use by market participants would maximise the value of the asset.

To protect its competitive position, or for other reasons, an entity may intend not to use an acquired non-financial asset actively or it may intend not to use the asset according to its highest and best use. Nevertheless, the entity shall measure the fair value of a non-financial asset assuming its highest and best use by market participants.

In the given case, the highest best possible use of the land is to develop a commercial complex. Although the developing a business complex is against the business objective of the entity, it does not affect the basis of fair valuation as IFRS 13 does not consider an entity specific restriction for measuring the fair value.

Also, its current use as a parking lot is not the highest best use as the land has the potential of being used for building a commercial complex.

Therefore, the fair value of the land is the price that would be received when sold to a market participant who is interested in developing a commercial complex.

- (ii) As per IFRS 13, unobservable inputs shall be used to measure fair value to the extent that relevant observable inputs are not available, thereby allowing for situations in which there is little, if any, market activity for the asset or liability at the measurement date. The unobservable inputs shall reflect the assumptions that market participants would use when pricing the asset or liability, including assumptions about risk.

In the given case, Dong Seng Limited adopted discounted cash flow method, commonly used technique to value shares, to fair value the shares of the private company as there were no similar shares traded in the market. Hence, it falls under Level 3 of fair value hierarchy.

Level 2 inputs include the following:

- (a) quoted prices for similar assets or liabilities in active markets.
- (b) quoted prices for identical or similar assets or liabilities in markets that are not active.
- (c) inputs other than quoted prices that are observable for the asset or liability.

If an entity can access quoted price in active markets for identical assets or liabilities of similar companies which can be used for fair valuation of the shares without any adjustment, at the measurement date, then it will be considered as observable input and would be considered as Level 2 inputs.

- 1.10 (i)** Paragraph 3 of IAS 20, Government Grants and Disclosure of Government Assistance, states that Government grants are assistance by government in the form of transfers of resources to an entity in return for past or future compliance with certain conditions relating to the operating activities of the entity. They exclude those forms of government assistance which cannot reasonably have a value placed upon them and transactions with government which cannot be distinguished from the normal trading transactions of the entity."

In accordance with the above, in the given case exemption of custom duty under EPCG scheme is a government grant and should be accounted for as per the provisions of IAS 20.

IAS 20 defines grant related to assets and grants related to income as follows:

“Grants related to asset are government grants whose primary condition is that an entity qualifying for them should purchase, construct or otherwise acquire long-term assets. Subsidiary conditions may also be attached restricting the type or location of the assets or the periods during which they are to be acquired or held.

Grants related to income are government grants other than those related to assets.”

In the given case, based on the terms and conditions of the scheme, the grant received is to compensate the import cost of assets subject to an export obligation as prescribed in the EPCG Scheme and does not relate to purchase, construction or acquisition of a long term asset. Hence it is a grant related to income.

#### **Accounting and Presentation of such grants**

It may be further noted that as per paragraph 12 of IAS 20, government grants shall be recognised in profit or loss on a systematic basis over the periods in which the entity recognises as expenses the related costs for which the grants are intended to compensate

Grants related to income are presented as part of profit or loss, over a period of six years, either separately or under a general heading such as ‘Other income’. Alternatively, they are deducted in reporting the related expense.

- (ii) (a) It seems that the equity shares are acquired for the purpose of selling it in the near term and therefore are held for trading. Such investments have been appropriately classified as subsequently measured at fair value through profit or loss. Such investments in equity shares cannot be classified as subsequently measured at fair value through other comprehensive income. The option to measure investment in equity shares at fair value through other comprehensive income has to be made at initial recognition. Therefore, equity shares that were held for trading previously cannot be reclassified to fair value through other comprehensive income due to change in business model to not held for trading.
- (b) In absence of contractual terms of NCDs, it is assumed that the contractual terms give rise on specified dates to cash flows that are solely payment of principal and interest on the principal outstanding. The business model also includes sales of these instruments on a regular basis. Hence, these instruments will be classified as FVTOCI. Therefore, such NCD investments shall be classified as subsequently measured at Fair Value through Other Comprehensive Income. The classification does not change based on whether the investment is current or non-current as the end of the reporting period. It

seems the company has previously classified these investments at fair value through profit or loss. The company must rectify this by reclassifying as FVT OCI.

**Question 2**

- 2.1 *Gold Limited and Copper Limited are partners of a joint operations engaged in the business of mining precious metals. The entity uses a jointly owned drilling plant in its operations.*

*During the year ended March 31, 2019 an inspection was conducted by the government authorities in the mining fields. The inspection authorities concluded that adequate safety measures were not followed by the entity. As a consequence, a case was filed and a penalty of ₹ 50 crores have been demanded from the Company.*

*The legal counsel of the company has assessed the demand and opined that appeals may not be useful and the appeal orders will be unfavourable to the joint venture. Out of ₹ 50 crores, ₹ 30 crore will be reimbursed by the Copper Limited, as per the terms of the Joint operations Agreement. As at the year end, actual reimbursement was not received from the Copper Limited. How will the liability be disclosed in the book of Gold Limited?*

- (A) As a provision for ₹ 20 crores and a contingent liability for ₹ 30 crores
- (B) As a contingent liability for ₹ 50 crores
- (C) As a provision for ₹ 30 crores and a contingent liability for ₹ 20 crores
- (D) As a provision for ₹ 50 crores

**(2 Marks)**

- 2.2 *A factory owned by ECL Limited was destroyed by fire. ECL Limited lodged an insurance claim for the value of the factory building, plant, and an amount equal to one year's net profit. During the year there were a number of meetings with the representatives of the insurance company.*

*Finally, before year-end, it was decided that ECL Limited would receive compensation for 90% of its claim. ECL Limited received a letter that the settlement cheque for that amount had been sent, but it was not received before year-end.*

*How should ECL Limited treat this in its financial statements?*

- (A) Record 90% of the claim as a receivable as it is virtually certain that the contingent asset will be received.
- (B) Do not make any adjustments in the financials and only disclose the contingent asset in the notes on accounts.
- (C) Wait until next year when the settlement cheque is actually received and not recognize or disclose this receivable at all since at year-end it is a contingent asset.
- (D) Record 100% of the claim as a receivable at year-end as it is virtually certain that the contingent asset will be received, and adjust the 10% next year when the settlement check is actually received.

**(2 Marks)**

2.3 Mittal Motors Limited is preparing financials for the year ended March 31, 2019. The Company had some queries in preparation of certain data that is required to be presented in the financials. As the retainer of the Company, please advise the company for the following issues:

- (i) Mittal Motors has issued 10,00,000 numbers of 9% cumulative preference shares. The Company has arrears of ₹ 15 crores of preference dividend as on March 31, 2019, it includes current year arrears of ₹ 1.75 crores. The Company did not declare any dividend for equity shareholders as well as for preference shareholders.

What is the amount of dividend to be reduced from profit or loss for the year for calculating basic Earnings Per Share?

(A) ₹ 15 crores

(B) ₹ 1.75 crores

(C) ₹ 13.25 crores

(D) Noting, as no dividend has been declared by the entity. **(2 Marks)**

- (ii) Further Mittal Motors has also issued certain convertible debentures, which are outstanding as at the year end. For the purposes of computation of weighted average number of shares (to arrive at diluted EPS) when should the dilutive potential shares should be deemed to have been converted into shares?

(A) At the start of the period.

(B) The date of issue of the potential shares

(C) At the start of the period or, if later, the date of the issue of the potential shares

(D) At the end of the period. **(2 Marks)**

2.4 Bharath Developers Limited are engaged in the business of developing Malls and leasing out them to its customers. The Company has an ongoing project in Kerala. It had borrowed ₹ 75 crores from a Bank to meet the project expenses.

- (i) The construction of the qualifying assets was suspended for a period of 10 days on completion of each floor for the concrete to settle. Further there was a delay of two months due to extreme floods in Kerala during which the active development of the project was interrupted.

There was a further delay of 15 days in completion due to rectification of the faulty electric wirings which was discovered during final inspection.

As the consultant of Bharath developers, advise the Company on, when the capitalisation of borrowing cost should be suspended ?

- (A) When there is a temporary delay for allowing the concrete to settle, which is a necessary part of the getting the asset ready for its intended use or sale.

- (B) During the extended period for rectifying faulty wires, in which active development is interrupted but substantial technical and administrative work is being carried out.
- (C) When all the activities necessary to prepare the Mall for its intended lease to customers are complete.
- (D) During the extended period in which active development is interrupted due to floods and substantial technical and administrative work is not being carried out.

**(2 Marks)**

- (ii) The Mall consisted of five phases. Bharath developers Limited has substantially completed all the work with regard to Phase I, II and III on March 5, 2019 and with regard to Phase IV and V on March 20, 2019.

The Company has carried out minor modifications based on specifications of the Lessee and handed over the shops to Lessees of Phase I, II and III on April 10, 2019 and to the lessees of Phase IV and V on April 15, 2019

Advise the Company on when it shall cease to capitalise the borrowing costs incurred with respect to the Mall ?

- (A) March 20, 2019 for the entire mall
- (B) April 15, 2019 for the entire mall
- (C) March 5, 2019 for Phase I, II and III; March 20, 2019 for Phase IV and V
- (D) April 10, 2019 for Phase I, II and III; April 15, 2019 for Phase IV and V

- 2.5 Boomerang Private Limited operates in the travel industry and incurs costs unevenly through the financial year. Advertising costs of ₹ 40 lacs were incurred on July 1, 2018, and staff bonuses are paid at year-end based on sales. Staff bonuses are expected to be around ₹ 400 lacs for the year; of that a sum of ₹ 60 lacs would relate to the period ending September 30, 2018.

What costs should be included in the entity's quarterly financial report for the quarter ended September 30, 2018 ?

- (A) Advertising costs ₹ 40 lacs; staff bonuses ₹ 100 lacs
- (B) Advertising costs ₹ 10 lacs; staff bonuses ₹ 100 lacs
- (C) Advertising costs ₹ 10 lacs; staff bonuses ₹ 60 lacs
- (D) Advertising costs ₹ 40 lacs; staff bonuses ₹ 60 lacs

**(2 Marks)**

- 2.6 Bijli Limited is engaged in the manufacturing and sale of electrical goods. It sells its goods on a warranty of 3 years. Normally 5% of customers claim on their warranty. The provision in the first quarter was calculated as 5% of sales to date, which was ₹ 100 lacs.

However, in the second quarter, a design fault was found and warranty claims were expected to be 10% for the whole of the year. Sales upto to the second quarter was ₹ 300 lacs. What would be the provision charged in the second quarter's interim financial statements ?

- (A) ₹ 30 lacs
- (B) ₹ 35 lacs
- (C) ₹ 25 lacs
- (D) ₹ 20 lacs

**(2 Marks)**

2.7 Indian Investments Limited purchased a trademark during the year ended March 31, 2019.

- (i) Indian Investments Limited had incurred the following cost in connection with the trade mark:

S. No.	Particulars	Amount (₹)
1.	One-time trademark purchase price	8,50,000
2.	Non-refundable taxes	38,000
3.	Training sales personnel on the use of the new trademark	45,000
4.	Research expenditures associated with the purchase of the new trademark	58,000
5.	Legal costs incurred to register the trademark	22,000
6.	Salaries of the administrative personnel	1,05,000

What is the value of trademark to be recognised in the books of Indian Investments Limited in accordance with IFRS ?

- (A) ₹ 11,18,000
  - (B) ₹ 10,73,000
  - (C) ₹ 9,55,000
  - (D) ₹ 9,10,000
- (ii) You are the IFRS consultant for the company. Out of the following disclosures given by Indian Investments Limited, advice the company which disclosure is not required under relevant IFRS ?
- (A) Fair value of similar intangible assets used by its competitors.
  - (B) Reconciliation of carrying amount at the beginning and the end of the year.
  - (C) Contractual commitments for the acquisition of intangible assets.
  - (D) Useful lives of the intangible assets.

**(2 Marks)**

- 2.8 Power India Limited issued 9% cumulative preference shares of ₹ 10 each on September 15, 2012 which are redeemable after 10 years.

You are appointed as the IFRS consultant of Power India Limited. Evaluate whether the preference shares are in nature of financial liability or equity instrument. Also, state the treatment of dividend paid to the preference shareholders under IFRS. **(4 Marks)**

- 2.9 Mathur India Private Limited has to present its first financials under IFRS for the year ended March 31, 2019. The transition date is April 1, 2017.

The following adjustments were made upon transition to IFRS :

- (a) The Company opted to fair value its land as on the date on transition.  
The fair value of the land as on April 1, 2017 was ₹ 10 crores. The carrying amount as on April 1, 2017 under the existing GAAP was ₹ 4.5 crores.
- (b) The Company has recognised a provision for proposed dividend of ₹ 60 lacs and related dividend distribution tax of ₹ 18 lacs during the year ended March 31, 2017. It was written back as on opening balance sheet date.
- (c) The Company fair values its investments in equity shares on the date of transition. The increase on account of fair valuation of shares is ₹ 75 lacs.
- (d) The Company has an Equity Share Capital of ₹ 80 crores and Redeemable Preference Share Capital of ₹ 25 crores.
- (e) The reserves and surplus as on April 1, 2017 before transition to IFRS was ₹ 95 crores representing ₹ 40 crores of general reserve and ₹ 5 crores of capital reserve acquired out of business combination and balance is surplus in the Retained Earnings.
- (f) The company identified that the preference shares were in nature of financial liabilities.

What is the balance of total equity (Equity and other equity) as on April 1, 2017 after transition to IFRS. Show reconciliation between total equity as per existing GAAP and as per IFRS to be presented in the opening balance sheet as on April 1, 2017. Ignore deferred tax impact. **(6 Marks)**

- 2.10 (i) Uttar Pradesh State Government holds 60% shares in PQR Limited and 55% shares in ABC Limited. PQR Limited has two subsidiaries namely P Limited and Q Limited. ABC Limited has two subsidiaries namely A Limited and B Limited. Mr. KM is one of the Key management personnel in PQR Limited.

- (a) Determine the entity to whom exemption from disclosure of related party transactions is to be given. Also examine the transactions and with whom such exemption applies. **(4 Marks)**
- (b) What are the disclosure requirements for the entity which has availed the exemption ? **(2 Marks)**



- (ii) KRR Enterprises Limited grants 150 shares to each employee on April 1, 2017. There were 300 employees as on that date. The shares will vest in the following manner:
- As on March 31, 2018 if the profit for the year increases 15% more than the profit for the year ended March 31, 2017 Or
  - As on March 31, 2019 if the Profit for the year ended March 31, 2018 increases 10% more than the profit for the year ended March 31, 2017.

The employees should remain in service during the vesting period.

The fair value per share as on the grant date is ₹325. The Profit for the year ended March 31, 2018 increased by 12% as compared to the profit for the year ended March 31, 2017.

During the year ended March 31, 2018, 25 employees left the organisation. Also, it was predicted that further 35 employees will leave in the following year. However, only 28 employees left during the year ended March 31, 2019.

Determine the employee benefit expenses to be accounted each year. Also, pass the necessary journal entries. **(4 Marks)**

2.11 Following is the balance sheet of Kuber Limited for the year ended March 31, 2019

**(₹ in lacs)**

	2019	2018
<b>ASSETS</b>		
<b>Non current Assets</b>		
Property, plant and equipment	13,000	12,500
Intangible assets.	50	30
Other financial assets	145	170
Deferred Tax Asset (net)	855	750
Other non-current assets	800	770
<b>Total Non-current assets</b>	<b><u>14,850</u></b>	<b><u>14,220</u></b>
<b>Current Assets</b>		
Financial assets		
Investments	2,300	2,500
Cash and cash equivalents	220	460
Other current assets	195	85
<b>Total Current assets</b>	<b><u>2,715</u></b>	<b><u>3,045</u></b>
<b>Total Assets</b>	<b><u>17,565</u></b>	<b><u>17,265</u></b>

<b>EQUITY AND LIABILITIES</b>		
<i>Equity</i>		
Equity share capital	300	300
Other equity	<u>12,000</u>	<u>8,000</u>
<b>Total equity</b>	<b><u>12,300</u></b>	<b><u>8,300</u></b>
<b>Liabilities</b>		
<b>Non current liabilities</b>		
Long term borrowings	2,000	5,000
Other non current liabilities	<u>2,740</u>	<u>3,615</u>
<b>Total non current liabilities</b>	<b><u>4,740</u></b>	<b><u>8,615</u></b>
<i>Current liabilities</i>		
<i>Financial liabilities</i>		
Trade payables	150	90
Bank Overdraft	75	60
Other current liabilities	300	200
<b>Total current liabilities</b>	<b><u>525</u></b>	<b><u>350</u></b>
<b>Total liabilities</b>	<b><u>5,265</u></b>	<b><u>8,965</u></b>
<b>Total Equity and Liabilities</b>	<b><u>17,565</u></b>	<b><u>17,265</u></b>

Additional Information:

- (1) Profit for the year ended March 31, 2019 - ₹ 4,450 lacs
- (2) Interim Dividend paid during the year - ₹ 450 lacs
- (3) Depreciation and amortisation charged in the statement of profit and loss during the current year are as under
  - (a) Property, Plant and Equipment - ₹ 500 lacs
  - (b) Intangible Assets - ₹ 20 lacs
- (4) During the year ended March 31st 2019 two machineries were sold for ₹ 70 lacs. The carrying amount of these machineries as on March 31, 2019 is ₹ 60 lacs.
- (5) Income taxes paid during the year ₹ 105 lacs

Using the above information of Kuber Limited, construct a statement of cash flows under indirect method.

**(10 Marks)**

**Answer to Question No. 2**

2.1 A

2.2 A

2.3 (i) B

(ii) C

2.4 (i) D

(ii) C

2.5 D

2.6 C

2.7 (i) D

(ii) A

2.8 In determining whether a preference share is a financial liability or an equity instrument, an issuer assesses the particular rights attached to the share to determine whether it exhibits the fundamental characteristic of a financial liability or an equity instrument.

(A) Redeemable preference shares at a specified date:

This contains a financial liability because the issuer has an obligation to transfer financial assets to the holder of the share. The potential inability of an issuer to satisfy an obligation to redeem a preference share when contractually required to do so, whether because of a lack of funds, a statutory restriction or insufficient profits or reserves, does not negate the obligation. Hence, classified as 'financial liability'.

(B) Distributions on preference shares

Another important point for consideration is whether the company has an obligation to make payments of dividend ie, whether dividend on such preference shares are cumulative or non-cumulative.

Where dividends are cumulative, one needs to assess the key terms of the instrument to check if the entity has a contractual obligation. In cases where the preference shares entitled to dividend which is payable such that entity does not have an unconditional right to defer payment, then this provides the shareholders with a lender's return on the amount invested. This obligation is also not negated if the entity is unable to pay such dividend for lack of funds or insufficient distributable profits. Therefore, the obligation to pay dividend meets the definition of financial liability.

**Conclusion:** In the given case, 9% Cumulative Preference shares redeemable after 10 years provides for mandatory fixed dividend payments and redemption of preference shares by Power India Ltd. for a fixed amount at a fixed future date. Since there is a contractual obligation to deliver cash (for both dividends and repayment of

principal) to the preference shareholder that cannot be avoided, the instrument is a financial liability in its entirety.

#### **Treatment of dividend paid to preference shareholders under IFRS**

The classification of a financial instrument as a financial liability or an equity instrument determines whether interest, dividends, losses and gains relating to that instrument are recognised as income or expense in profit or loss. Interest, dividends, losses and gains relating to a financial instrument or a component that is a financial liability shall be recognised as income or expense in profit or loss.

Since the preference shares are classified as financial liability, the dividend thereon will be considered in the nature of interest and accordingly be charged to Profit and Loss as part of finance cost.

#### **2.9 Computation of balance total equity as on April 1, 2017 after transition to IFRS**

			₹ in crore
Share capital- Equity share Capital			80
Other Equity			
General Reserve		40	
Capital Reserve		5	
Retained Earnings (95-5-40)	50		
Add: Increase in value of land (10-4.5)	5.5		
Add: De recognition of proposed dividend (0.6 + 0.18)	0.78		
Add: Increase in value of Investment	<u>0.75</u>	<u>57.03</u>	<u>102.03</u>
Balance total equity as on April 1, 2017 after transition to IFRS			<u>182.03</u>

#### **Reconciliation between Total Equity as per existing GAAP and IFRS to be presented in the opening balance sheet as on 1<sup>st</sup> April, 2017**

		₹ in crore
Equity share capital (80+25)		80
Redeemable Preference share capital		<u>25</u>
		105
Reserves and Surplus		<u>95</u>
Total Equity as per existing GAAP		200
Adjustment due to reclassification		
Preference share capital classified as financial liability		(25)

Adjustment due to derecognition		
Proposed Dividend not considered as liability as on 1 <sup>st</sup> April 2017		0.78
Adjustment due to re-measurement		
Increase in the value of Land due to re-measurement at fair value	5.5	
Increase in the value of investment due to re-measurement at fair value	<u>0.75</u>	<u>6.25</u>
Equity as on April 1, 2017 after transition to IFRS		<u>182.03</u>

- 2.10 (i) (a)** As per para 18 of IAS, 'Related Party Disclosures', if an entity has had related party transactions during the periods covered by the financial statements, it shall disclose the nature of the related party relationship as well as information about those transactions and outstanding balances, including commitments, necessary for users to understand the potential effect of the relationship on the financial statements.

However, as per para 25 of the standard a reporting entity is exempt from the disclosure requirements in relation to related party transactions and outstanding balances, including commitments, with:

- (i) a government that has control or joint control of, or significant influence over, the reporting entity; and
- (ii) another entity that is a related party because the same government has control or joint control of, or significant influence over, both the reporting entity and the other entity

According to the above paras, for Entity P's financial statements, the exemption in paragraph 25 applies to:

- (i) transactions with Government Uttar Pradesh State Government; and
- (ii) transactions with Entities PQR and ABC and Entities Q, A and B.

Similar exemptions are available to Entities PQR, ABC, Q, A and B, with the transactions with UP State Government and other entities controlled directly or indirectly by UP State Government. However, that exemption does not apply to transactions with Mr. KM. Hence, the transactions with Mr. KM needs to be disclosed under related party transactions.

- (b) It shall disclose the following about the transactions and related outstanding balances referred to in paragraph 25:
  - (a) the name of the government and the nature of its relationship with the reporting entity (ie control, joint control or significant influence);
  - (b) the following information in sufficient detail to enable users of the entity's

financial statements to understand the effect of related party transactions on its financial statements:

- (i) the nature and amount of each individually significant transaction; and
- (ii) for other transactions that are collectively, but not individually, significant, a qualitative or quantitative indication of their extent.

(ii)

Note:

In the absence of the information regarding the profit % for the year ended 31<sup>st</sup> March, 2019, it may be either assumed that the company's earnings increased to desired level and the performance target has been met or *vice versa*.

According to first assumption i.e. "the company's earnings increased to desired level and the performance target has been met", the solution will be as follows:

Since the earnings of the entity is non-market related, hence it will not be considered in fair value calculation of the shares given. However, the same will be considered while calculating number of shares to be vested.

**Determination of expenses for each year ended on:**

		2018	2019
a	Total employees	300	300
b	Cumulative- Employees left (Actual)	(25)	(53)
c	Employees expected to leave in the next year	(35)	(-)
d	Year end – No. of employees (a-b-c)	240	247
e	Shares per employee	150	150
f	Fair value of share at grant date	325	325
g	Vesting period	1/2	2/2
h	Cumulative expenses (d x e x f x g)	58,50,000	1,20,41,250
i	Expenses to be recognised (h-h of previous year)		61,91,250

#### Journal Entries

31 <sup>st</sup> March, 2018	₹	₹
Employee benefits expenses Dr.	58,50,000	
To Share based payment reserve (equity)		58,50,000
(Equity settled shared based payment expected vesting amount)		

Profit and Loss A/c	Dr.	58,50,000	
To Employee benefits expenses (Employee benefits expenses transferred to P&L A/c)			58,50,000
31 <sup>st</sup> March, 2019			
Employee benefits expenses	Dr.	61,91,250	
To Share based payment reserve (equity) (Equity settled shared based payment expected vesting amount)			61,91,250
Profit and Loss A/c	Dr.	61,91,250	
To Employee benefits expenses (Employee benefits expenses transferred to P&L A/c)			61,91,250
Share based payment reserve (equity)	Dr.	1,20,41,250	
To Share Capital (150 x 247 x 100*)			37,05,000
To Securities Premium A/c (Share capital Issued)			83,36,250

\*Assumed that each share was of ₹ 100 each.

**Alternatively**, it is assumed that the company's earnings had not increased to desired level and the performance target has not been met. In such a situation, the answer would be same except the last entry for transfer of share based payment reserve which will be as follows:

Share based payment reserve (equity)	Dr.	1,20,41,250	
To General reserve (In case of non-vesting of awards, transfer of SBP reserve to another equity)			1,20,41,250

## 2.11

**Statement of Cash Flows**

		₹ in lacs
<i>Cash flows from Operating Activities</i>		
Net Profit after Tax	4,450	
Add: Tax Paid	<u>105</u>	
	4,555	
Add: Depreciation & Amortisation (500 + 20)	520	
Less: Gain on Sale of Machine (70-60)	<u>(10)</u>	

Less: Increase in Deferred Tax Asset (855-750)	<u>(105)</u>	
	4,960	
Change in operating assets and liabilities		
Add: Decrease in financial asset (170 - 145)	25	
Less: Increase in other non-current asset (800 - 770)	(30)	
Less: Increase in other current asset (195 - 85)	(110)	
Less: Decrease in other non-current liabilities (3,615 - 2,740)	(875)	
Add: Increase in other current liabilities (300 - 200)	100	
Add: Increase in trade payables (150-90)	<u>60</u>	
	4,130	
Less: Income Tax	<u>(105)</u>	
Cash generated from Operating Activities		4,025
<i>Cash flows from Investing Activities</i>		
Sale of Machinery	70	
Purchase of Machinery [13,000-(12,500 - 500-60)]	(1,060)	
Purchase of Intangible Asset [50-(30-20)]	(40)	
Sale of Financial asset - Investment (2,500 - 2,300)	<u>200</u>	
Cash outflow from Investing Activities		(830)
<i>Cash flows from Financing Activities</i>		
Dividend Paid	(450)	
Long term borrowings paid (5,000 - 2,000)	<u>(3,000)</u>	
Cash outflow from Financing Activities		<u>(3,450)</u>
Net Cash outflow from all the activities		(255)
Opening cash and cash equivalents (460 - 60)		<u>400</u>
Closing cash and cash equivalents (220 - 75)		<u>145</u>

**Note:**

1. It is assumed that other non-current/current assets and liabilities are related to operations of Kuber Ltd. and do not contain any element of financing and investing activities.
2. Further, profit for the year given in the question is assumed as profit after tax. Hence non-cash adjustment of defer tax has been done.



Alternatively, it may be assumed that profit given in the question is profit before tax. In such a situation, the solution will be as follows:

**Statement of Cash Flows**

		₹ in lacs
<i>Cash flows from Operating Activities</i>		
Net Profit before Tax	4,450	
Add: Depreciation & Amortisation (500 + 20)	520	
Less: Gain on Sale of Machine (70-60)	<u>(10)</u>	
	4,960	
Change in operating assets and liabilities		
Add: Decrease in financial asset (170 - 145)	25	
Less: Increase in other non-current asset (800 - 770)	(30)	
Less: Increase in other current asset (195 - 85)	(110)	
Less: Decrease in other non-current liabilities (3,615 - 2,740)	(875)	
Add: Increase in other current liabilities (300 - 200)	100	
Add: Increase in trade payables (150-90)	<u>60</u>	
	4,130	
Less: Income Tax	<u>(105)</u>	
Cash generated from Operating Activities		4,025
<i>Cash flows from Investing Activities</i>		
Sale of Machinery	70	
Purchase of Machinery [13,000-(12,500 - 500-60)]	(1,060)	
Purchase of Intangible Asset [50-(30-20)]	(40)	
Sale of Financial asset - Investment (2,500 - 2,300)	<u>200</u>	
Cash outflow from Investing Activities		(830)
<i>Cash flows from Financing Activities</i>		
Dividend Paid	(450)	
Long term borrowings paid (5,000 - 2,000)	<u>(3,000)</u>	
Cash outflow from Financing Activities		<u>(3,450)</u>
Net Cash outflow from all the activities		(255)
Opening cash and cash equivalents (460 - 60)		<u>400</u>
Closing cash and cash equivalents (220 - 75)		<u>145</u>

**Question No.3**

3.1 *Mirage India Private Limited is planning to dispose of a collection of assets during the year ended March 31, 2018. The entity designates these assets as a disposal group, and the carrying amount of these assets immediately before classification as held for sale was ₹75,00,000.*

- (i) *Upon being classified as held for sale the assets were valued to ₹ 68,00,000. However, subsequently the Company also received an external valuation at ₹60,00,000.*

*How would the reduction in the value of the assets on classification as held for sale be treated in the financial statements?*

- (A) *The entity recognises a loss of ₹ 15,00,000 immediately before classifying the disposal group as held for sale.*  
(B) *The entity recognises an impairment loss of ₹15,00,000.*  
(C) *The entity recognises an impairment loss of ₹7,00,000.*  
(D) *The entity recognises a loss of ₹ 7,00,000 immediately before classification as per relevant IFRS and then recognises a loss of ₹8,00,000 against assets held for sale.* **(2 Marks)**

- (ii) *Out of the assets classified as held for sale there were machineries for which active market was not available at present. Mirage India Private Limited anticipates that it might take 2 more years to sell the asset in the market. Meanwhile the strategy team of the company had found that the assets can be leased out to contractors for short term. Thus, these machineries no longer satisfy the criteria of an asset held for sale.*

*Suggest the suitable treatment for the aforesaid machinery out of the following:*

- (A) *Continue to measure the machineries at their current carrying value.*  
(B) *Measure the machineries at lower of their carrying amount before the asset was classified as held for sale (as adjusted for subsequent depreciation, amortisation, or revaluations) and its recoverable amount at the date of the decision not to sell.*  
(C) *Re-measure the machineries at their fair value.*  
(D) *Recognise the machineries at their carrying amount prior to its classification as held for sale as adjusted for subsequent depreciation, amortisation, or revaluations.*

3.2 *Nickel Private Limited acquired 100% of Coal Private Limited, on January 1,2018.*

- (i) *The fair value of the purchase consideration was ₹ 10 crores consisting of ordinary shares of ₹100 each of Nickel. The fair value of the net assets acquired was ₹7.5 crores. At the time of the acquisition, the value of the ordinary shares of Nickel and the net assets of Coal were only provisionally determined.*

On November 30, 2018 it was finally determined that the fair value of Nickel's Shares was ₹11 crores and the fair value of net assets of Coal was ₹8 crores.

However, the directors of Nickel have seen the fair value of the company's shares decline since January 1, 2018, and wanted to adopt the fair value of the shares as of February 1, 2019, which will result in the fair value of consideration at being valued at ₹9 crores.

What is the value of purchase consideration and fair value of net assets of Coal Private Limited as at the date of acquisition ?

- (A) Purchase consideration ₹11 crores, net asset value ₹8 crores.
- (B) Purchase consideration ₹10 crores, net asset value ₹7.5 crores.
- (C) Purchase consideration ₹9 crores, net asset value ₹8 crores.
- (D) Purchase consideration ₹11 crores, net asset value ₹7.5 crores. **(2 Marks)**

- (ii) In addition to the above purchase consideration, the acquisition agreement states that an additional ₹2 crores will be paid if Coal Private Limited achieves a turnover of ₹80 crores in the next two years. On the date of acquisition, the fair value of the said consideration was ₹1.50 crores. In February 2019, due to Coal's declining performance it is determined that it is unlikely that it would meet budgeted turnover of ₹80 crores.

How should Nickel treat the above consideration?

- (A) Nickel should not recognise the consideration as it is unlikely that it would be paid.
- (B) Nickel should disclose the consideration as its contingent liability in its financial statements as it is a contingent liability which will be met only upon Coal Private Limited earning a turnover ₹80 crores.
- (C) Nickel should recognize the fair value of consideration as part of the business combination, thus increasing goodwill and remeasure it at the end of each reporting period. The impact of change in fair value is recognized in the statement of profit and loss.
- (D) There is no specific treatment prescribed under IFRS. Nickel should decide the appropriate accounting treatment based on the facts and circumstances of the case. **(2 Marks)**

- 3.3 Thermal Solutions Limited started its business in India with Indian Rupee as its functional currency. After several years, the entity expanded and started exporting its product to Europe. By the end of March 31, 2019, 90% of the business was conducted with Europe and the transaction were denominated in Euro. The raw materials required (for the products to be exported to Europe) are all imported materials and the purchase transactions are

denominated in Euro. (Whereas during the year ended March 31, 2018 only 30% of the business was conducted in Euro).

What will be the functional currency of Thermal Solutions Limited for the year 2018-19?

- (A) Changed to euro at the end of financial year 2018-19, if it is considered that the underlying transactions, events and conditions of business have changed.
- (B) Changed to euro at the beginning of financial year 2018-19, if it is considered that the underlying transactions, events and conditions of business have changed
- (C) Changed to euro at the end of financial year 2017-18, if it is considered that the underlying transactions, events and conditions of business have changed.
- (D) The functional currency remains to be Indian Rupee.

3.4 Himanshu Limited acquired 100% of the share capital of Global Tech Limited for a consideration of 20 million EURO on September 30, 2018. The fair value of the net assets of Global Tech at that date was 11 million EURO. The functional currency of Himanshu is Indian Rupee. The exchange rates as on September 30, 2018 was 85 INR/EURO and on March 31, 2019 was 89 INR/EURO. What is the value of goodwill in the books of Himanshu Limited as on March 31, 2019?

- (A) 765 million INR
- (B) 935 million INR
- (C) 800 million INR
- (D) 801 million INR

**(2 Marks)**

3.5 Blueberry Limited manufactures various types of chocolates. A common base mixture is prepared in a huge mixing bowl from where it is sent through pipes to various compartments of machine for adding flavouring agents and other ingredients and then poured into moulds. The chocolates are then packed neatly by the machine and which are in turn sealed in cartons and then are sent through trucks for distribution. The various types of chocolate include Vanilla filling, strawberry filling, cashew chew, roasted almond, fruit and nut, crunchy crackle, the classic, jelly belly, etc. Each of the flavours are performing well individually and were contributing significantly towards the Company's revenue.

Should the Company classify these different types of chocolates into different segments?

- (A) Yes, the Company should classify these different types of chocolates into different segments as they contribute significantly towards the Company's revenue.
- (B) No, the given information is not adequate to determine whether these different types of chocolates should be classified as different segments.
- (C) No, there is no need to create different segments for each type of chocolate the nature of the product, production process, type of customers and the method of distribution are common.

- (D) Yes, the Company should classify these different types of chocolates into different segments as they consist of different raw materials, have their own customer base and are capable of generating significant revenue individually. **(2 Marks)**
- 3.6 A portion of a mall is renovated by constructing a food court, spa and gaming zone so as to increase the footfalls in the mall. The food court and gaming zone are expected to result in a significant increase in sales for the shops and outlets of the mall. What should be the accounting treatment for the cost incurred for the renovation ?
- (A) Expenses incurred for food court and gaming zone should be charged to statement of profit and loss;
- (B) Expenses incurred for food court, spa and gaming zone should be charged to statement of profit and loss;
- (C) Expenses incurred for food court, spa and gaming should be capitalised;
- (D) Expenses incurred for food court and gaming should be capitalised. **(2 Marks)**
- 3.7 Dharam Limited has spent ₹ 15 lacs in developing a new product during the year ended March 31, 2019. The development costs incurred were recognised as an intangible asset in accordance with IAS 38. For the purposes of computing the taxable income, these expenses are allowable in full in the year of incurring the expenses. At the year end, the Company recognised an impairment loss of ₹75,000 against the intangible asset. What is the tax base of the intangible asset?
- (A) ₹ 15,00,000
- (B) ₹ 75,000
- (C) ₹ 14,25,000
- (D) ₹ 0 **(2 Marks)**
- 3.8 Ind AS 40 is not applicable to which of the following properties:
- (A) Held under Finance lease and leased out under an operating lease;
- (B) Held under finance lease and leased out under finance lease;
- (C) Property acquired with a view for development and resale;
- (D) Property occupied by Employees paying rent at less than market rate. **(2 Marks)**
- 3.9 Answer the following questions with reference to appropriate IFRS :
- (i) C Tech Solutions Limited is engaged in the business of developing software. It has a customary business practice of requiring both a signed license agreement and a purchase order/contract.
- A Limited approached C Tech Solutions to purchase their product X. A Limited issued a purchase order for purchase of the product and related Product Customisation Services (PCS) prior to the period ended March 31, 2019. Due to non availability of the authorised person, A Limited has not signed the purchase order / contract till

March 31, 2019. A Limited had already installed the software X in its employee's system and C Tech Limited had also started providing PCS services prior to March 31, 2019.

Evaluate whether revenue can be recognised under IFRS 15. **(3 Marks)**

- (ii) Planes India Limited had agreed to build a jet for a customer. The consideration to build the jet includes a fixed price of ₹15 crores plus a completion bonus of ₹50 lacs if completed within two months prior to May 30, 2019 (agreed date of completion as per the contract with customer). The contract also includes a performance bonus of ₹0 to 50 lakhs depending on the number of flights of the jet during its first year of operation by the customer.

How will the transaction price of the contract be determined? **(7 Marks)**

3.10 Durable Industries India Limited is a renowned company known for its care towards employees.

- (i) Durable Industries contributes to an industrial pension plan that provides a pension arrangement for its employees. It is a popular plan among the employers of the same industry. The Company does not have any obligation other than payment of annual contribution. Under this scheme the contribution is received from various employers and it is in turn used to compensate the employee of those companies after their retirement. Identify the nature of the above employee benefit plan with reference to IFRS. **(3 Marks)**

- (ii) Durable Industries previously had a defined pension plan (a defined benefit plan) under which the employees who joined before April 1, 2012 were enrolled. With respect to employees who joined on or after April 1, 2012 were all enrolled in the industrial pension plan. The Company found that the industrial pension plan was more beneficial to the employees than the defined pension plan. Hence, during 2018-19 it decided to change all the employees from defined pension plan to the industrial pension plan. The entity paid ₹5 crore to the employees who in turn agreed to forfeit the pension entitlement from the defined pension plan. The liability recognised in the financials, for the year ended March 31, 2018, with respect to the pension liability was ₹7 crores.

How should this be accounted in the financials for the year ended March 31, 2019? **(3 Marks)**

- (iii) Supreme developers Limited, Southern Constructions Limited and Concrete India Limited jointed together to develop a project of luxurious holiday villas along the back waters of Bay of Bengal.

The land for the project was arranged by Supreme developers. Concrete India Limited supplied the raw materials like Cement, bricks, stones, rods, required for construction. Southern Constructions Limited took care of the labour required for construction of villas and interior decoration.

*The common costs like site approval, registration, site preparation is borne equally by all the three parties.*

*In the contractual agreement it was mentioned that the profit from sale of villa will be shared equally after setting off the expenses incurred for developing the project.*

*Identify the type of joint arrangement as per IFRS. (4 Marks)*

- 3.11 (i) *Sumeru Limited holds 35% of total equity shares of Meru Limited, an associate company. The value of Investments in Meru Limited on March 31, 2018 is ₹ 3 crores in the consolidated financial statements of Sumeru Limited.*

*Sumeru Limited sold goods worth ₹ 3,50,000 to Meru Limited. The cost of goods sold is ₹ 3,00,000. Out of these goods worth ₹ 1,00,000 were in the closing stock of Meru Limited.*

*During the year ended March 31, 2019 the profit and loss statement of Meru Limited showed a loss of ₹ 1 crore.*

(A) *What is the value of investment in Meru Limited as on March 31, 2019 in the consolidated financial statements of Sumeru Limited, if equity method is adopted for valuing the investments in associates ?*

(B) *Will your answer be different if Meru Limited had earned a profit of ₹ 1.50 crores and declared a dividend of ₹ 75 lacs to the equity shareholders of the Company?*

**(6 Marks)**

- (ii) *Tee Limited is carrying on the business of developing light weight and medium weight guns for the Indian defence industry. Tee Limited acquired 48% of shares in Kay Limited, a company engaged in advanced research in weapons. Tee Limited acquired shares in Kay Limited to substantiate their position in the industry.*

*The remaining 52% of shares are held by the key management personnel of the Company Kay Limited. The Kay management consists of eleven people who are experts in the fields of advanced weapons and the core of the Company.*

*Tee Limited has the option to purchase remaining 52% at any time by paying 6 times the market price of the share. But on purchase of the shares it is highly possible that the key management personnel will leave the company.*

(A) *State whether Tee Limited has control over Kay Limited.*

(B) *What will be your answer if Tee Limited had 51% of shares in Kay Limited and Kay Limited can start the research, development and production of weapon only with the stringent approval process of the defence ministry of the Central Government.*

**(4 Marks)**

**Answer to Question No. 3**

3.1 (i) D

(ii) B

3.2 (i) A

(ii) C

3.3 A

3.4 D

3.5 C

3.6 C

3.7 D

3.8 B, C and D

3.9 (i) In order to recognise revenue under IFRS 15, an entity has to apply following steps viz-

**Step 1: Identify the contract with the customer**

To apply the model in IFRS 15, an entity must first identify the contract, or contracts, to provide goods and services to customers. A contract must create enforceable rights and obligations to fall within the scope of the model in the standard. Such contracts may be written, oral or implied by an entity's customary business practices. The fact that it normally obtains written agreement does not necessarily mean that an oral agreement is not a contract. For example, if an entity has an established practice of starting performance based on oral agreements with its customers, it may determine that such oral agreements meet the definition of a contract.

As a result, an entity may need to account for a contract as soon as performance begins, rather than delay revenue recognition until the arrangement is documented in a signed contract. Certain arrangements may require a written contract to comply with laws or regulations in a particular jurisdiction. These requirements must be considered when determining whether a contract exists.

In the given case, since the software has already been installed in the employee's system of the customer and had also started providing PCS services prior to 31<sup>st</sup> March, 2019, it appears that enforceable rights and obligations exists.

**Attributes of a contract**

To determine whether (and when) the arrangements with customers are contracts within the scope of the model in the standard, following attributes must be present:

- The parties have approved the contract and are committed to perform their respective obligations.



- Each party's rights regarding the goods or services to be transferred can be identified.
- Payment terms can be identified.
- The contract has commercial substance.
- It is probable that the entity will collect the consideration to which it will be entitled in exchange for the goods or services that will be transferred to the customer.

**Step 2: Identify the performance obligations in the contract.**

Performance obligation is installation of software in the employee's system and procurement of product customization services (PCS)

**Step 3: Determine the transaction price.**

This is to predict the total amount of consideration to which the entity will be entitled from the contract. For the purpose of determining the transaction price, an entity shall assume that the goods or services will be transferred to the customer as promised in accordance with the existing contract and that the contract will not be cancelled, renewed or modified.

Here the goods and services have been delivered or performed.

An entity shall consider the terms of the contract and its customary business practices to determine the transaction price.

**Step 4: Allocate the transaction price to the performance obligations in the contract.**

An entity shall allocate the transaction price to each performance obligation identified in the contract on a relative stand-alone selling price i.e. delivering of goods and providing product customization services are two separate elements and revenue should be separately recognised for both the elements.

In the given case, there are two performance obligations one delivery of software and another is PCS services.

**Step 5: Recognize revenue when (or as) the entity satisfies its performance obligations.**

An entity transferred the product i.e. installed the software at point in time. However, service is performed over the point of time.

Therefore, revenue with respect to delivery of software can be recognised if all the five models of IFRS 15 are met while revenue with respect to PCS will be recognised on satisfying the performance obligation over time as per the terms of the contract.

**(ii) Determine the transaction price**

An entity shall consider the terms of the contract and its customary business practices to determine the transaction price. The transaction price is the amount of consideration to which an entity expects to be entitled in exchange for transferring promised goods or services to a customer, excluding amounts collected on behalf of third parties (for example, some sales taxes). The consideration promised in a contract with a customer may include fixed amounts, variable amounts, or both.

If the consideration promised in a contract includes a variable amount, an entity shall estimate the amount of consideration to which the entity will be entitled in exchange for transferring the promised goods or services to a customer.

**Estimating variable consideration**

An entity is required to estimate variable consideration using either the 'expected value' or the 'most likely amount' method, as described in the standard:

An entity shall estimate an amount of variable consideration by using either of the following methods, depending on which method the entity expects to better predict the amount of consideration to which it will be entitled:

- (a) The expected value—the expected value is the sum of probability-weighted amounts in a range of possible consideration amounts. An expected value may be an appropriate estimate of the amount of variable consideration if an entity has a large number of contracts with similar characteristics.
- (b) The most likely amount—the most likely amount is the single most likely amount in a range of possible consideration amounts (ie the single most likely outcome of the contract). The most likely amount may be an appropriate estimate of the amount of variable consideration if the contract has only two possible outcomes (for example, an entity either achieves a performance bonus or does not).

An entity is required to choose between the expected value method and the most likely amount method based on which method better predicts the amount of consideration to which it will be entitled. That is, the method selected is not meant to be a 'free choice'. Rather, an entity selects the method that is best suited, based on the specific facts and circumstances of the contract.

**Conclusion:** In the given case, the contract includes both a fixed and a variable price as consideration. Hence the transaction price is equal to fixed consideration plus variable consideration.

The fixed consideration agreed is ₹ 15 crore.

The completion bonus of ₹ 50 lacs and performance bonus of ₹ Nil to 50 lacs would be considered as variable elements present in the contract while determining the transaction price.

The entity prepares a separate estimate for each element of variable consideration to which the entity will be entitled using the estimation methods described in IFRS 15 as below:

- (a) The entity should use the most likely amount to estimate the variable consideration associated with the completion bonus. This is because there are only two possible outcomes (₹ 50 lacs or nothing) and it is the method that the entity would expect to better predict the amount of consideration to which it will be entitled. The company can estimate the time of completion of constructing the jet.
- (b) The entity should use the expected value method to estimate the variable consideration associated with the broad range of performance bonus (ie based on number of flights taken up during the first year of operation). This is because it is the method that the entity would expect to better predict the amount of consideration to which it will be entitled.

- 3.10 (i)** Under defined contribution plans, an entity agrees to contribute a limited amount to the fund as its legal or constructive obligation. Thus, the amount of the post-employment benefits received by the employee is determined by the amount of contributions paid by an entity (and perhaps also the employee) to a post-employment benefit plan or to an insurance company, together with investment returns arising from the contributions; and as a result of this, actuarial risk (which means that benefits will be less than expected) and investment risk (that assets invested will be insufficient to meet expected benefits) falls on the employee and not on the entity like in defined benefit plan.

Further Multi-employer plans are defined contribution plans (other than state plans) or defined benefit plans (other than state plans) that:

- (a) pool the assets contributed by various entities that are not under common control; and
- (b) use those assets to provide benefits to employees of more than one entity, on the basis that contribution and benefit levels are determined without regard to the identity of the entity that employs the employees.

In the given case, Durable Industries alongwith other employees contribute to the plan and the plan pays the pension to the employees on retirement from the common pool of the asset. Also the company has no obligation after contributing annually to the industrial pension plan. Hence, it is a multi-employer plan under the defined contribution scheme.

- (ii) The discontinuation of old defined pension plan is a curtailment event. Durable Industries is supposed to recognise gain or loss on settlement when the legally binding agreement has been reached, that eliminates all further legal or constructive

obligations for the benefits provided under the pension plan in exchange for lump sum payment.

As per para 109 of IAS 19 'Employee Benefits', the gain or loss on a settlement is the difference between:

- (a) the present value of the defined benefit obligation being settled, as determined on the date of settlement
- (b) the settlement price, including any plan assets transferred and any payments made directly by the entity in connection with the settlement.

Accordingly, Durable Industries recognises a settlement gain of ₹ 2 crore (ie ₹ 7 crore – ₹ 5 crore) in its financial statements for the year ended 31<sup>st</sup> March, 2019.

**(iii) Paragraphs 15-17 of IFRS 11 state as follows:**

A joint operation is a joint arrangement whereby the parties that have joint control of the arrangement have rights to the assets, and obligations for the liabilities, relating to the arrangement. Those parties are called joint operators.

A joint venture is a joint arrangement whereby the parties that have joint control of the arrangement have rights to the net assets of the arrangement. Those parties are called joint venturers.

An entity applies judgement when assessing whether a joint arrangement is a joint operation or a joint venture. An entity shall determine the type of joint arrangement in which it is involved by considering its rights and obligations arising from the arrangement. An entity assesses its rights and obligations by considering the structure and legal form of the arrangement, the terms agreed by the parties in the contractual arrangement and, when relevant, other facts and circumstances.

As per para B16 of the standard, a joint arrangement that is not structured through a separate vehicle is a joint operation. In such cases, the contractual arrangement establishes the parties' rights to the assets, and obligations for the liabilities, relating to the arrangement, and the parties' rights to the corresponding revenues and obligations for the corresponding expenses.

In the present case, the arrangement among Supreme Developers Limited, Southern Constructions Limited and Concrete India Limited is not structured through a separate vehicle. All the three entities have joint control over the arrangement of land, supply of material and labour for the purpose of construction activity ie development project of luxurious holiday villas. They will be sharing profit from sale of villas and common costs and also incur their own separate costs. Accordingly, the arrangement is a joint operation.

- 3.11 (i) (a) **Value of investment in Meru Ltd. as on 31<sup>st</sup> March, 2019 as per equity method in the consolidated financial statements of Sumeru Ltd.**

	₹
Cost of Investment	3,00,00,000
Less: Share in Post-Acquisition Loss (1,00,00,000 x 35%)	(35,00,000)
Less: Unrealised gain on inventory left unsold with Meru Ltd. $\{[(50,000/3,00,000) \times 1,00,000] \times 35\}$	<u>(5,833)</u>
Carrying value as per Equity method	<u>2,64,94,167</u>

- (b) **Value of investment in Meru Ltd. as on 31<sup>st</sup> March, 2019 as per equity method in the consolidated financial statements of Sumeru Ltd.**

	₹
Cost of Investment	3,00,00,000
Add: Share in Post-Acquisition Profit (1,50,00,000 x 35%)	52,50,000
Less: Unrealised gain on inventory left unsold with Meru Ltd. $\{[(50,000/3,00,000) \times 1,00,000] \times 35\}$	<u>(5,833)</u>
Less: Dividend (75,00,000 x 35%)	<u>(26,25,000)</u>
Carrying value as per Equity method	<u>3,26,19,167</u>

**Note:** In the absence of clarity in the information that whether unsold inventory is the cost value for Sumeru or Meru Ltd., the above solution has been given considering that ₹1,00,000 is the cost price of the inventory for Sumeru Ltd.

**Alternatively,** if it is considered as cost price to Meru Ltd. then the solution will be as follows:

- (a) **Value of investment in Meru Ltd. as on 31<sup>st</sup> March, 2019 as per equity method in the consolidated financial statements of Sumeru Ltd.**

	₹
Cost of Investment	3,00,00,000
Less: Share in Post-Acquisition Loss (1,00,00,000 x 35%)	(35,00,000)
Less: Unrealised gain on inventory left unsold with Meru Ltd. $\{[(50,000/3,50,000) \times 1,00,000] \times 35\}$	<u>(5,000)</u>
Carrying value as per Equity method	<u>2,64,95,000</u>

(b) Value of investment in Meru Ltd. as on 31st March, 2019 as per equity method in the consolidated financial statements of Sumeru Ltd.	
	₹
Cost of Investment	3,00,00,000
Add: Share in Post-Acquisition Profit (1,50,00,000 x 35%)	52,50,000
Less: Unrealised gain on inventory left unsold with Meru Ltd. [[{(50,000/3,50,000) x 1,00,000} x 35%]	(5,000)
Less: Dividend (75,00,000 x 35%)	<u>(26,25,000)</u>
Carrying value as per Equity method	<u>3,26,20,000</u>

(ii) As per para 7 of IFRS 10, an investor controls an investee if and only if the investor has all the following:

1. Power over the investee

Further, as per para 10 of the standard, an investor has power over an investee when the investor has existing rights that give it the current ability to direct the relevant activities, ie the activities that significantly affect the investee's returns.

2. Exposure, or rights, to variable returns from its involvement with the investee

As per para 15 of the standard, an investor is exposed, or has rights, to variable returns from its involvement with the investee when the investor's returns from its involvement have the potential to vary as a result of the investee's performance.

3. The ability to use its power over the investee to affect the amount of the investor's returns

An investor is exposed, or has rights, to variable returns from its involvement with the investee when the investor's returns from its involvement have the potential to vary as a result of the investee's performance. The investor's returns can be only positive, only negative or both positive and negative.

Based on the above guidance, following can be concluded:

(a) Tee limited has acquired 48% in Kay Limited. The purpose of acquiring the shares by Tee limited in it is to substantiate their position in the industry. Kay Limited is a specialist entity that is engaged in advanced research in weapons. Acquiring Kay Limited will help Tee limited to gain access to their research which would complement Tee limited's operations and business of developing light weight and medium weight guns.

The key management personnel who holds 52% shares of Kay Limited are key for running Kay Limited's business of advanced research and will help

Tee limited to acquire the market through ground breaking advanced researches of Kay Limited. In case of acquisition of 52% stake of Kay Limited, the key management personnel may leave the organisation and in such a situation Tee limited will not enjoy any economic benefit or infact will lose the benefit of unique technical knowledge of those 11 experts.

Hence, Tee limited would not be able to use its power over Kay Limited to affect the amount of its returns which is one of the essential criteria to assess the control, so there is no control of Tee limited on Kay Limited.

- (b) Even though Tee limited has acquired 51% stake in Kay Limited yet it does not have power over Kay Limited as it would not be able to exercise its existing rights that give it the current ability to direct the relevant activities, ie the activities that significantly affect the investee's returns. In other words, the relevant activity of Kay Limited is advance research in weapons which will help Tee limited to substantiate their position. However, the research, development and production will start only after stringent approval process of the defence ministry of the Central Government. Thus regulations prevent Tee limited to direct the relevant activity of Kay Limited which ultimately lead to prevent Tee Limited to have control.